SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 40 1 4 3

GATH P. FREEMAN, Trustee under the Will and of the Estate of Henry C. Starr, Deceased,

Appellant,

vs.

GILBERT K. HEWITT, Director of Gross Income Tax Division, Department of Treasury, State of Indiana.

APPEAL FROM THE SUPREME COURT OF THE STATE OF INDIANA.

APPELLANT'S REPLY BRIEF

Gath P. Freeman,
Counsel for Appellant.

INDEX

Subject Index

Subjects:	Page
Intangibles Are Subjects of Commerce	1
The State of the Buyer, But Not That of the Seller, Is Privileged to Tax	2
Cases Cited or Discussed by Appellee	5
The Gross Income Tax of Indiana Is Laid Directly on Gross Receipts from Interstate Commerce	7
Multiplicity of Tax Burdens	8

Authorities Cited

Cases:	
Adams (J. D.) Mfg. Co. v. *Storen*, (1938) 304 U. S. 307, 58 Sup. Ct. 913	1,7
Chicago Board of Trade v. *Olsen*, (1922) 262 U. S. 1	2
Dept. of Treasury v. *Wood Preserving Corp.*, (1941) 313 U. S. 62, 61 Sup. Ct. 885	6
General Trading Co. v. *State Tax Com.*, (1944) 322 U. S. 335, 64 Sup. Ct. 1028	6
International Harvester Co. v. *Dept. of Treasury*, (1944) 322 U. S. 435, 64 Sup. Ct. 1019	5,6
McGoldrick v. *Berwind-White Coal Mining Co.*, (1940) 309 U. S. 33, 60 Sup. Ct. 388	10
McLeod v. *Dilworth Co.*, (1944) 322 U. S. 327, 64 Sup. Ct. 1023	4,6
Southern Pacific Co. v. *Gallagher*, (1939) 306 U. S. 167	7
U. S. v. *Southeastern Underwriters Assn.*, (1944) 322 U. S. 533	5
Law Review:	
57 Harvard Law Review 40	5,11

Statutes

Indiana Intangibles Tax Act, Summary (Ch. 81, Indiana Acts 1933, p. 523; Burns Indiana Statutes, 1943 Replacement, Sec. 64-901)	11
Burns Indiana Statutes, 1943 Replacement, Sec. 64-2602, Sec. 2, Ch. 117, Indiana Acts 1937, p. 611	7

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 40

GATH P. FREEMAN, TRUSTEE UNDER THE WILL AND OF THE ESTATE OF HENRY C. STAIR, DECEASED,
Appellant,

vs.

GILBERT K. HEWITT, DIRECTOR OF GROSS INCOME TAX DIVISION, DEPARTMENT OF TREASURY, STATE OF INDIANA,
Appellee

APPEAL FROM THE SUPREME COURT OF THE STATE OF INDIANA

APPELLANT'S REPLY BRIEF

1

Intangibles Are Subjects of Commerce

After seriously contending in the lower courts that intangibles were not proper subjects of commerce or interstate commerce and that the case of *J. D. Adams Manufacturing Company* v. *Storen* (1938), 304 U. S. 307, 58 Sup. Ct. 913, and cases following it were inapplicable to

this case, on the ground that such decisions concerned tangible property only (Appellant's Brief, pp. 30, 31; R. 24, 26, 28, 29, 30) the appellee now for the first time concedes that intangibles "may be subjects of commerce between the states" (Appellee's Brief, p. 11), but the appellee qualifies that admission by saying that "It is possible to argue that Appellant's transactions in regard to his stocks and bonds did not constitute interstate commerce" (Appellee's Brief, pp. 11, 12). The appellee cites the case of *Chicago Board of Trade* v. *Olsen* (1922), 262 U. S. 1, 32, in which it was held that sales of grain futures were not in themselves interstate commerce although they could be and were regarded by Congress as directly interfering with interstate commerce (Appellee's Brief, p. 12). The appellee does not explain the pertinence of that decision, which seems quite obscure, but is content to drop the subject and to rely wholly on that case for authority that appellant's sales of his stocks and bonds did not constitute interstate commerce. The case cited seems so devoid of any probative value in support of appellee's contention that it would appear fair to charge that the appellee thereby concedes that the sales by appellant of his stocks and bonds constituted interstate commerce within the meaning of the commerce clause.

2

The State of the Buyer, But Not That of the Seller, Is Privileged to Tax

In this connection the appellee states that "It would appear appellant has misconstrued the decisions of this court" (Appellee's Brief, p. 9).

While the appellant carried a heading to that effect in his original brief, page 17, it was obvious from the argument immediately following that the same was not a generalization or pronouncement of the appellant, but of the

Supreme Court of Indiana in its opinion in this case (R. 30, 34) (Appellant's Brief, p. 17).

The appellant does not understand that the Supreme Court of the United States has adopted or applied any such general rule, which of necessity would be entirely arbitrary. The complexity of the subject of state taxation of interstate commerce or of taxable events in connection therewith or incident thereto, in view of the decided cases, is such that the pronouncement of a general rule of application within the spirit and intent of the commerce clause, and at the same time allowing the states any privileges of such taxation, would seem to be beyond the realm of possibility. Although the rationale of the decisions in favor of taxes levied by the state of the buyer is on a sounder foundation in logic and reason and supportable by sound practical considerations, nevertheless some forms of taxes may be levied by the state of the seller, as for instance a tax measured by gross receipts which is in lieu of a general property tax and fairly apportioned, and perhaps others. (57 Harvard Law Review 40, 82.) While for practical purposes and to avoid confusion and uneconomical impediments to interstate commerce, and to apply the principles of taxation, which seem to be more in favor of taxation by the state of the buyer than by that of the seller, it might seem warranted or advisable to adhere to a general rule that the state of the buyer and not that of the seller may tax interstate commerce transactions, it is not the province of the appellant to proclaim such a rule, and the appellant respectfully submits that he did not intend to do so. It might be well if all acts of the states in taxing interstate commerce were replaced by an act of Congress, with reasonable apportionment to the states on some fair and equal basis of general and uniform application throughout the United States, which would seem to accord with the letter, spirit and intent

of the Constitution. But the parties to this action are not concerned with political economy or philosophy of government, but only with the constitutional law under the commerce clause as developed and established by this court.

The very purpose of the commerce clause was to secure and maintain free trade among the several states, *McLeod v. J. E. Dilworth Co.*, 322 U. S. 327, 64 Sup. Ct. 1023, 1026, and in view of the ramifications and complexities of the innumerable types of state taxes invented to provide state revenue and to circumvent the commerce clause, and the resultant confusion and impediments to and burdens upon interstate commerce, it might appear advisable to adhere to a general rule or arbitrary formula that the state of the buyer but not that of the seller may tax, if either be permitted to do so, and let the states accommodate their tax laws thereto. This would provide the states with revenue, would have the virtue of at least partial uniformity of application and at the same time require interstate commerce "to bear its share of the tax burden."

To one engaged in buying and selling or holding securities for investment purposes, or for legitimate speculation, it seems of little importance that a tax imposed upon his selling of securities in interstate commerce is not greater than he would be required to pay upon an intrastate sale. The state has the right to burden its internal commerce with taxes, within constitutional bounds, but not to illegally burden interstate commerce. The imposition of the gross income tax of Indiana upon the receipts from sales of intangibles in interstate commerce at the rate of one per cent involves a substantial tax liability each year and precludes the making of many sales in commerce between the state of Indiana and other states not only by appellant but by many other residents of Indiana, thereby reducing the volume of such commerce and thwarting and hampering the same contrary to and in violation of the commerce clause. A larger

rate of tax could and would destroy all such commerce. And the taxation of gross receipts, or equivalent taxes in both the state of the buyer and the seller would undoubtedly accomplish the same result.

This court has never sanctioned the imposition of taxes measured by gross receipts in both the state of the buyer and the state of the seller on the same interstate transaction. *International Harvester Co.* v. *Department of Treasury*, 322 U. S. 435, 64 Sup. Ct. 1019, 1023. 57 Harvard Law Review 40, 70, 72-74, 82.

3

Cases Cited or Discussed by Appellee

All of the cases cited or discussed by the appellee in his brief which concern interstate commerce or which throw any light on the issue here involved were cited or discussed by the appellant in his original brief, except those mentioned and discussed as follows:

The case of *United States* v. *Southeastern Underwriters Association* (1944), 322 U. S. 533 (Appellee's Brief, p. 17), was an action by the United States Government under the Sherman Anti Trust Act and did not involve state taxation of interstate commerce, but it was held therein that the trafficking in insurance contracts across state lines constituted interstate commerce subject to regulation by Congress.

All the other cases above referred to, cited by the appellee in his brief and which concern interstate commerce transactions and the taxing thereof, are in accord with the decision of the *Adams* case and in no wise at variance with it. In fact the *Adams* case is cited with approval in several of those cases. The appellee has cited no case which is inconsistent with the decision of the *Adams* case, and this appellant, in a careful search for authorities, has found none.

In the case of *International Harvester Co.* v. *Department of Treasury* (1944), 322 U. S. 335, 64 Sup. Ct. 1019, supra, all of the sales described in the several classes were consummated on deliveries made in Indiana, "transactions consummated within the borders of Indiana," and the court sustained the tax as applied thereto (Appellee's Brief, pp. 5, 9, 10). The same is true of *Department of Treasury* v. *Wood Preserving Corp.* (1941), 313 U. S. 62, 61 Sup. Ct. 885. (Appellee's Brief p. 10.) Thus they are readily distinguishable from the *Adams* case and the case at bar.

In the case of *McLeod* v. *Dilworth Co.* (1944), 322 U. S. 327, 64 Sup. Ct. 1023, supra (Appellee's Brief, pp. 5, 9, 10), this court held, in agreement with the Supreme Court of Arkansas, in condemning the tax, that the sale there involved was different from that in the *Berwind-White Coal Mining Co.* case in that the sale, the transfer of ownership, was consummated on delivery in Tennessee, the state of the seller, to the Arkansas purchaser, whereas in the *Berwind-White* case the Pennsylvania seller completed his sales in New York, where the seller maintained offices and took orders, and that "for Arkansas to impose a tax on such transactions would be to project its powers beyond its boundaries and to tax an interstate transaction." This case appears to have little or no probative value in the case at bar, except as to general principles involved in such transactions. While the appellee asserts that "the facts were practically identical with the facts in the *Adams* case" (Appellee's Brief, p. 5), there is really no similarity in fact.

The same can be said of *General Trading Co.* v. *State Tax Com.* (1944) 322 U. S. 335, 64 Sup. Ct. 1028, (Appellees' Brief, p. 11), which sustained a use tax of Iowa on property purchased and delivered in interstate sales from Minneapolis on orders taken by salesmen in Iowa approved by the home office in Minnesota, whence the goods were shipped into Iowa.

The case of *Southern Pacific Co.* v. *Gallagher* (1939), 306 U. S. 167, (Appellee's Brief, p. 12), is another use tax case, wherein a use tax of California was upheld on shipments from out-of-state into California by the Southern Pacific Co. of its property for its use in said state.

All of said cases cited by the appellee involved taxes of the state of the buyer, or sales consummated in the taxing state by a resident buyer or by a non-resident buyer in the taxing state, except the *McLeod* case above differentiated, and except the *Adams* case, which was also cited by appellee.

Like the *Adams* case, the sales in the case at bar were made by a resident of Indiana to purchasers residing in other states, in this case consummated on deliveries made in New York, in the *Adams* case consummated on deliveries made in other states and foreign countries. The sales were not consummated in Indiana, as in the *International Harvester* and *Wood Preserving Corp.* cases.

The Gross Income Tax of Indiana Is Laid Directly On Gross Receipts From Interstate Commerce

The appellee asserts that "in *Adams Manufacturing Co.* v. *Storen* (1938), 304 U. S. 307, 310-311, this court erroneously rejected the characterization by the Indiana Supreme Court of the Indiana Gross Income Tax as a tax upon residents based upon the privilege of domicile." (Appellee's Brief, p. 6.)

The statute imposes the tax upon the "receipt of gross income, measured by the amount or volume of gross income, and in the amount to be determined by the application of rates on such gross income * * *". (Burns Indiana Statutes, 1943 Replacement, Sec. 64-2602; Sec. 2, Ch. 117, Indiana Acts 1937, p. 611; Appellant's Brief, Appendix A, p. 45.) The statute applies alike to persons domiciled in Indiana

and to non-residents, so far as the receipts of gross income derived from activities or businesses or any other source within the state is concerned. So it can hardly be contended that the tax is based on the "privilege of domicile."

In the *Adams* case the Attorney General said in his brief that it was a privilege tax upon the receipt of gross income; the regulations of the Department of Treasury, pursuant to authority granted by the Act, treated the exaction as a gross receipts tax, and this court held it to be such a tax in the following language:

> "We conclude that the tax is what it purports to be—a tax upon gross receipts from commerce. Appellant's sales to customers in other states and abroad are interstate and foreign commerce. The Act, as construed, imposes a tax of one per cent. on every dollar received from these sales." 58 Sup. Ct. 913, 915, 916.
>
> . . . . . .
>
> "We hold that, as respects the appellant's sales of its manufactured product in interstate and foreign commerce, the statute cannot constitutionally be enforced." 58 Sup. Ct. 913, 917.

5

Multiplicity of Tax Burdens

The appellee assumes and asserts that "Since the mere possibility of multiplicity of taxes is no longer to be considered as an invalidating factor, this rationale of the *Adams* case is not here applicable." (Appellee's Brief, p. 6.) Previously (Appellee's Brief, p. 5) the appellee says that "The rationale of the *Adams* case, if not repudiated by this court, is at least subject to serious question," because, as the appellee says, "One major premise of that case was that the interstate features of the transactions involved were exposed to the danger of a multi-

plicity of taxes by the several states in which the component parts of the commerce occurred," and that "This premise no longer exists." The appellee cites the case of *McLeod v. Dilworth Co., supra,* in support thereof, which is not in point, because in that case the tax in the state of the buyer, Arkansas, was condemned for the reason that the sale was held to have been consummated on delivery in the state of the seller, Tennessee, as hereinabove discussed. To regard the *McLeod* case as authority for appellees' proposition would be to disregard the decision in the *Berwind-White* case, *supra.* The case was decided on the ground that the sale was consummated in Tennessee, not in Arkansas.

The appellee also cites the *International Harvester Co.* case, *supra,* 64 Sup. Ct. 1019, in support of this proposition, saying that in that case "this court specifically held that where the record discloses no tax upon the same event by another state the mere possibility of such a tax will not invalidate the tax already levied and that as to the invalidation of a tax by reason of a multiplicity of levies '* * * it will be time to cross that bridge when we come to it.'" (Appellee's Brief, pp. 5, 6.)

It would seem that the appellee wholly misunderstood the holding of this court in that respect. The opinion of the court and the tax there involved concerned "Class D" sales which were sales by an Indiana seller, International Harvester Co., of Indiana goods to an out-of-state buyer who comes to Indiana, takes delivery there and transports the goods to another state. 64 Sup. Ct. 1019, 1021. The court held that both the agreement to sell and the delivery took place in Indiana and that those events would be adequate to sustain a sales tax by Indiana, citing the *Berwind-White* case and other authorities, and in conclusion the court said:

> "Much is said, however, of double taxation, particularly with reference to the Class D sales. It is argued

that appellants will in all probability be subjected to the Illinois Retailers' Occupation Tax for some of those sales * * *. But it will be time to cross that bridge when we come to it. * * * But we did not withhold the hand of Indiana's tax collector on that account. Nor is the problem like that of an attempted tax on the gross proceeds of an interstate sale by both the State of the buyer and the State of the Seller. Cf. J. D. Adams Mfg. Co. v. Storen, supra. We only hold that where a State seeks to tax gross receipts from interstate transactions consummated within its borders its power to do so cannot be withheld on constitutional grounds where it treats wholly local transactions the same way. Such 'local activities or privileges' (McGoldrick v. Berwind-White Coal Co., supra, 309 U. S. at page 58, 60 Sup. Ct. at page 398 * * *) are as adequate to support this tax as they would be to support a sales tax. To deny Indiana this power would be to make local industry suffer a competitive disadvantage:" 64 Sup. Ct. 1019, 1023.

For the appellee to argue that the appellant did not pay any tax upon his transactions in any other state is begging the question. It is obvious that taxes paid by either the buyer or the seller levied on interstate commerce transactions do burden, thwart, discourage, hamper and prevent such commerce, varying in degree in proportion to the amount of tax, whether paid by the seller, the buyer or both. If the taxes are in excess of taxes legally levied by a state on local commerce in a similar transaction they are illegal burdens and unconstitutional. Taxes levied by the state of the seller measured by the full sales price upon an interstate transaction have been uniformly condemned, with certain exceptions hereinbefore noted (for instance, a tax measured by gross receipts in lieu of a general property tax), and under the practical approach as now applied by the court such a tax imposed by the state of the buyer is sustained, *McGoldrick* v. *Berwind-White Coal Mining Co.*,

supra, in which case the court stressed the nondiscriminatory effect of the sales tax which equalized the tax burden between interstate and intrastate sales. But this would not be true if the seller's state could likewise impose such a tax on the same interstate sale. Unlike a tax on transportation, there is no practicable basis on which to apportion a sales price between the seller's and the buyer's state. 57 Harvard Law Review 40, 69, and Note 138.

There was no evidence in the *Adams* case that any tax was paid to or in any other state by the seller, the J. D. Adams Mfg. Co., or by the buyers of its products. But it is common knowledge that all states have tax laws taxing both tangible and intangible property and/or the use and/or the income and/or the receipts thereof or therefrom.

The state of Indiana has an Intangibles Tax Act enacted in the year 1933 (Ch. 81, Indiana Acts 1933, p. 523; Burns Indiana Statutes, 1943 Replacement, Sec. 64-901), which in definition is a privilege tax required to be paid by every person, including among others fiduciaries and trustees, residing in or domiciled in the state for the right to exercise any one or more of the privileges therein enumerated, including among others the right of selling, assigning, transferring, renewing, removing, consigning, mailing, shipping, trading in and enforcing intangibles, which by definition in the Act include among others promissory notes, stocks in foreign corporations, bonds and debentures. The Act recites, Sec. 64-931, that the tax imposed shall be in lieu of all other taxes except estate and/or inheritance and gross income taxes which might have been or might be imposed upon intangibles or against the owners or holders thereof by virtue of any prior law.

Prior to the enactment of the Intangibles Tax Act intangibles were subject to the general property tax laws. The intangibles tax is in lieu of the property tax but in

practical effect is a property tax, but the gross income tax is not.

There is nothing to prevent any other state from enacting an intangibles tax law similar to the Indiana Act, and it is fair to assume, without any evidence in the record of this case, that all states have tax laws taxing intangibles based on their value or sales price and/or the receipts and income therefrom.

The Indiana intangibles tax, which is levied immediately on purchase or acquiring of intangibles, is tantamount to a sales tax because it is defined in the Act as a tax on the privilege of the owner of selling intangibles and because upon the purchasing or acquiring of intangibles from out-of-state the tax immediately attaches on delivery to the purchaser and is payable in ten days thereafter, with penalties for default. Thus the State of Indiana already has two sales taxes on sales of intangibles, which, if the gross income tax stands as a valid tax, unduly burden interstate commerce, to the extent at least that they are in excess of the amount imposed on intrastate sales. Corporate stocks and bonds maturing in more than one year are called annual intangibles, the tax paid upon purchase or acquiring is for one year thereafter, and the tax is payable within ten days after each succeeding annual anniversary. The tax is 5¢ on each $20.00 of the actual value or fractional part thereof of each annual intangible, represented by stamps attached thereto.

On purchase the value is measured by the market or sales price.

If an Indiana resident sells to another Indiana resident, there is only the gross income tax payable on the transaction, not the intangibles tax, but if he sells interstate to a resident of another state having such or similar intangibles taxes there is that tax on the transaction in the state of

the buyer in addition to the gross income tax of Indiana paid by the seller. Sales of intangibles are subject to sales taxes, or taxes which are tantamount to or the equivalent of sales taxes, in the state of the buyer or where the sale is consummated, in the same or similar fashion as sales of tangible property for consumption or use, so far as the commerce clause is concerned.

If an owner sells a security and reinvests the proceeds in another security purchased out-of-state, without the Indiana intangibles tax paid thereon, he is liable again, immediately on purchase, for the intangibles tax on the reinvestment of the same capital, as well as for gross income tax on the receipts from each sale. This is true *ad infinitum*.

If other states have similar tax laws, which they do have or could have, can it be said with any plausibility that such taxes in the state of the buyer coupled with the gross income tax of Indiana in the state of the seller do not illegally burden interstate commerce?

The operation of the Indiana intangibles tax in this connection is so similar in effect to that of a sales tax that the difference, if any, is in name and not in substance.

It is evident that any state may have a sales tax or equivalent tax on sales of securities, with equal and similar burdening effect on interstate commerce as on sales of tangible property.

The appellee still clings to his theory of situs (Appellee's Brief, pp. 9-15) although it is not clear from the argument just what the theory is.

On sales of tangible property the situs for purposes of taxation changes at the place of delivery and consummation of sale to a new situs, and on sales of intangible property the situs likewise changes at the place of delivery and consummation of sale from the place of domicile of the seller to that of the buyer. In the case of tangible prop-

erty the delivery is of the things sold, or perhaps of a bill-of-sale, bill of lading or title papers of some kind. In the case of stocks and bonds the delivery is of the stock certificates assigned for transfer of the shares evidenced thereby or of the bonds evidencing the debt. Does the appellee mean that there can be no sale consummated within the meaning of the commerce clause unless the buyer takes actual physical possession of the thing purchased?

The appellee and the State do not construe the Intangibles Tax Act in such manner, but hold that the intangibles tax attaches immediately on purchase by and delivery to an Indiana resident. The purchase and delivery is consummated in case of stocks and bonds by the delivery to the Indiana purchaser of the stock certificates and bonds, whereupon the situs of the corporate stock evidenced thereby or bonds, as the case may be, changes to the place of domicile in Indiana of the purchaser. There is no doubt about that. And likewise there is no doubt that in selling stocks or bonds interstate by an Indiana resident the situs changes to the place of domicile of the purchaser in another state upon consummation of sale and delivery of the stock certificates or bonds.

In case of securities sold through the New York Stock Exchange the delivery and consummation of sale is made in New York according to the rules and regulations of said Exchange, but the purchaser may be domiciled in any state or in a foreign country.

The appellee surely does not contend that the situs remains with the seller even after consummation of sale and delivery of the securities sold. Surely the state of the buyer, or the state where the sale is consummated, can lay a tax thereon to the same extent and with the same effect as in case of tangible property.

Conclusion

The appellant respectfully submits that for aught that appears in appellee's brief and for the reasons hereinabove and in appellant's original brief set forth, the decision of the Supreme Court of Indiana in this case should be reversed.

Respectfully submitted,

GATH P. FREEMAN,
Attorney for Appellant.